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No. 06-666

FILED
JUL 19 2007
OFFICE OF THE CLERK
SUPREME COURT, U.S.

In The Supreme Court of the United States

DEPARTMENT OF REVENUE OF THE COMMONWEALTH OF KENTUCKY and FINANCE AND ADMINISTRATION CABINET OF THE COMMONWEALTH OF KENTUCKY,

Petitioners,

v.

GEORGE W. DAVIS and CATHERINE V. DAVIS,

Respondents.

On Writ Of Certiorari To The Court Of Appeals Of Kentucky

JOINT APPENDIX

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Certiorari Granted May 21, 2007

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The following opinions and orders have been omitted in printing this Joint Appendix because they appear on the following pages in the appendix to the Petition for Certiorari:

Jefferson Circuit Court's Order Granting Summary Judgment ..... Pet. App. A15

Opinion of the Court of Appeals of Kentucky, *Davis v. Department of Revenue*, 193 S.W.3d 557 (Ky. App. 2006) ..... Pet. App. A1

Order of the Supreme Court of Kentucky Denying Motion for Discretionary Review ..... Pet. App. A14

RELEVANT DOCKET ENTRIES

Circuit Court, Division I
Jefferson County, Commonwealth of Kentucky

Civil Action No. 03-CI-03282

George W. Davis, et al.,
Plaintiffs
vs.
Revenue Cabinet, Commonwealth of Kentucky, et al.,
Defendants

04/11/2003	Case Filed CONTRACT *JURY FEE NOT PAID*
04/11/2003	Document Filed COMPLAINT/PETITION AP
	* * *
05/05/2003	Document Filed ANSWER D *REVENUE CABINET*
	* * *
07/17/2003	Document Filed ORDER SETTING TRIAL/HEARING JUD *ORAL ARGUMENTS 9-29-03 @1:30*
	* * *
07/18/2003	Motion Filed MOTION FOR SUMMARY JUDGMENT ATTORNEY FOR DEFENDANT (CIVIL) *DEFT'S. . . . MEMO IN SUPPORT NO ORD. TEND.*

08/22/2003 Document Filed
MISCELLANEOUS
AP
PLTFS' OPPOSITION TO DEFTS' MOT. FOR SUM.JUDGMENT.

* * *

09/03/2003 Document Filed
MISCELLANEOUS
AP
PLTFS' OPPOSITION TO DEFTS' MOTION FOR SUM.JUDGMENT. BINDER I & II.

* * *

09/08/2003 Document Filed
ORDER FOR APPEARANCE PRO HAC VICE
TAMMY MCCLENDON STOKES AND DAVID J. GUINN ON BEHALF OF PLAINTIFFS, GEORGE W. DAVIS AND CATHERINE V. DAVIS

* * *

09/08/2003 Document Filed
ORDER FOR APPEARANCE PRO HAC VICE
M. SCOTT BARRETT, DONN H. WRAY, JOHN R. WYLIE, HART L. ROBINVITCH ON BEHALF OF PLAINTIFFS GEORGE W. DAVIS AND CATHERINE V. DAVIS

* * *

09/12/2003 Document Filed
REPLY
AD
DEFTS' . . . . TO PLTFS' OPPOSITION TO DEFTS' MOT. FOR SUM.JUDGMENT

* * *

09/29/2003 Scheduled Event Sep 29 2003 at 1:30 PM
ORAL ARGUMENTS
HON. BARRY WILLETT

10/17/2003 Document Filed
MISCELLANEOUS
AD
DEFT'S CONFIRMATION OF EXHIBIT OFFERED AT HEARING O[N] MOT. FOR SUM.JUDGMENT.

11/06/2003 Motion Filed
MOTION – OTHER
ATTORNEY FOR PLAINTIFF
PLTFS'. . . . COURT TO ENTER ORDER THAT CONFIRMATION OF RECEIPT OF 4/10/03. ORD. TEND.

* * *

11/10/2003 Document Filed
ORDER – OTHER
LETTERS OF 041003 ATTACHED TO PLAINTIFF'S MO. FOR ENTRY OF THIS ORDER REQ. INCOME TAX REFUND ON BEHALF OF PLAINTIFFS AND OTHERS SIMILARLY SITUATED OFFERED INTO EVIDENCE 041003, HEREBY MADE PART

04/15/2004 Motion Filed
MOTION TO FILE
ATTORNEY FOR PLAINTIFF
PLTFS'. . . . SUPPLEMENTAL AUTHORITY IN OPPOSITION TO DEFTS' MOT. FOR S.J. ORD. TEND.

* * *

04/20/2004 Document Filed
ORDER – OTHER
PLAINTIFF'S REQ. TO FILE SUPP. AUTH. IN OPP. TO DEF'S MO. FOR SJ IS SUSTAINED. COURT MAY IN ITS DELIBERATION WITH RESPECT TO SJ MO. CONSIDER SUCH AUTH. AND THE ARGUMENT OF PLAINTIFF'S COUNSEL

04/20/2004 NOE to All Counsel of Record and Parties Not Represented by Counsel.
ORDER – OTHER
FIRST CLASS MAIL
PLAINTIFF'S REQ. TO FILE SUPP. AUTH. IN OPP. TO DEF'S MO. FOR SJ IS SUSTAINED. COURT MAY IN ITS DELIBERATION WITH RESPECT TO SJ MO. CONSIDER SUCH AUTH. AND THE ARGUMENT OF PLAINTIFF'S COUNSEL

05/03/2004 Document Filed
RESPONSE
AD
DEFTS' . . . . TO PLTFS' SUPPLEMENTAL AUTHORITY.

08/30/2004 Case Disposed 507 Days
SUMMARY JUDGMENT
JURY FEE NOT PAID

08/30/2004 Document Filed
ORDER GRANTING
JUD
DEFENDANT'S MOTION FOR SJ

* * *

09/21/2004 Document Filed
NOTICE OF APPEAL
AP
$125.00 FEE PAID. COPIES MAILED TO: GEORGE M. GEOGHEGAN, III, CLERK, A. RALUY, M. BARRETT, D. TRAINOR, D. WRAY, H. ROBINOVITCH, C. WATKINS, J. WYLIE, M. DAMPIER, D. GUIN AND T. STOKES

* * *

12/14/2004 Document Filed
NOTICE OF CERTIFICATION OF RECORD ON APPEAL
CASE CRETIFIED [sic] *AND COPIES MAILED TO GEORGE M. GEOGHEGAN, III, CLERK AND TO IRVIN D. FOLEY DAVID W. GRAY, DOUG DOWELL, DEBRA KEELEN AND SEE INDEX CARD FOR THE REST OF ATTORNEYS.*

* * *

COURT OF APPEALS OF KENTUCKY
Appeal No. 2004-CA-001940-MR

#	Date	Description	Memo
1	08/30/2004	CIRCUIT COURT JUDGMENT: **JD**	
2	09/21/2004	NOTICE OF APPEAL – REGULAR CIVIL: **AI**	** FILING FEE PAID **Due Date: (10/11/2004)**
3	10/07/2004	PREHEARING STATEMENT: **HE**	**Due Date: 10/18/2004)**
		* * *	
7	10/22/2004	PREHEARING CONF SCHED DATE TIME LOCATION: **CS**	PREHEARING CONFERENCE 11/12/04 2:30 LOUISVILLE P.S.
8	11/15/2004	PREHEARING CONF RESULT (NO SETTLEMENT): **RC**	
9	11/15/2004	ORDER ENTERED TO START: **ST**	PREHEARING CONFERENCE ORDER – TIME FOR ALL FURTHER STEPS, SUBSEQUENT TO THE NOTICE OF APPEAL, SHALL COMMENCE TO [R]UN FROM THE ENTRY OF THIS ORDER, EXCEPT AS STATED BELOW: 1) THE APPELLANTS SHALL FILE THEIR BRIEF

			WITHIN SIXTY (60) DAYS FROM THE DATE THE RECORD IS CERTIFIED. (2) THE APPELLEES SHALL FILE ITS BRIEF WITHIN SIXTY (60) DAYS FROM THE DATE THE APPELLANT' BRIEF IS FILED. (3) THE APPELLANTS SHALL FILE THEIR REPLY BRIEF WITHIN FIFTEEN (15) DAYS FROM THE DATE THE APPELLEES' BRIEF IS FILED. **Due Date: (01/24/2005)**
10	12/14/2004	NOTIF. OF CERTIFICATION – REGULAR CIVIL: **NI**	**Due Date: (02/14/2005)**
11	02/14/2005	APPEAL PERFECTED: **AP**	**Due Date: (04/15/2005)**
12	04/05/2005	PROCEDURAL MOTION: **MP**	APPELLEE'S MOTION FOR ADDITIONAL TIME TO FILE BRIEF, UP TO AND INCLUDING MAY 16, 2005 **Due Date: (04/18/2005)**
		* * *	
14	04/21/2005	ORDER GRANTING PROCEDURAL MOTION: **OMPG**	COURT ORDER DELIVERED, GRANTING APPELLEE'S MOTION FOR ADDITIONAL TIME TO FILE BRIEF. APPELLEE'S BRIEF SHALL BE FILED ON

			OR BEFORE 5/16/05. **Due Date: (05/6/2005)**
15	05/13/2005	APPELLEE BRIEF FILED: **AB**	**Due Date: (05/31/2005)**
16	06/01/2005	PROCEDURAL MOTION: **MP**	APPELLANT'S MOTION FOR ADDITIONAL TIME TO FILE REPLY BRIEF, 30 DAYS, UP TO AND INCLUDING JULY 15, 2005. TIMELY MAILED REGISTERED MAIL 05-31-05. **Due Date: (06/13/2005)**
		* * *	
18	06/17/2005	ORDER GRANTING PROCEDURAL MOTION: **OMPG**	COURT ORDER DELIVERED, GRANTING APPELLANT'S MOTION FOR ADDITIONAL TIME TO FILE A REPLY BRIEF. BRIEF SHALL BE FILED ON OR BEFORE 6/30/05. **Due Date: (06/30/2005)**
19	07/01/2005	APPELLANT'S REPLY BRIEF:**RB**	FILED TIMELY PURSUANT TO CR.76.40 (2) – SENT REGISTERED MAIL ON 6/30/05.
20	07/01/2005	RECORD REQUEST FROM CIRCUIT COURT CLRK: **RR**	**Due Date: (08/01/2005)**

21	07/20/2005	RECORD FILED: **RF**	2 VOLUMES RECORD
22	07/22/2005	SUBMISSION: **R3**	
23	08/16/2005	APPEAL ASSIGNED ON THE MERITS: **SH1**	ASSIGNED MONTH: 12/2005 PRESIDING JUDGE: MINTON JOHN D. PANEL: 2. NOTE:
24	10/07/2005	ASSIGN/ SCHEDULE (DATE, TIME & LOCATION) **SH2**	DATE: 12/02/2005 TIME: 11:00 AM LOCATION: JEFFERSON COUNTY JUDICIAL CENTER, 10TH FLOOR APPELLATE COURTROOM, 700 WEST JEFFERSON, LOUISVILLE, KENTUCKY NOTE:
25	11/17/2005	PROCEDURAL MOTION: **MP**	IRVIN FOLEYS MOTION FOR JOHN WYLIE TO BE ADDED PRO HAC VICE COUNSEL FOR APPELLANTS. (1 COPY TO MZ, 2 COPIES TO JS) **Due Date: (11/28/2005)**
26	11/18/2005	RESPONSE TO MOTION: **ZZM**	APPELLEE'S RESPONSE TO IRVIN FOLEY'S MOTION FOR JOHN WYLIE TO BE ADDED PRO HAC VICE COUNSEL FOR APPELLANT'S. (1 COPY TO MZ)

* * *

28	12/01/2005	ORDER GRANTING PROCEDURAL MOTION: **OMPG**	COURT ORDER DELIVERED GRANTING MOTION BY IRVIN D. FOLEY TO ADMIT JOHN R. WYLIE TO PRACTICE PRO HAC VICE ON BEHALF OF APPELLANTS.
29	01/06/2006	OPINION – VACATING & REMANDING: **P6**	OPINION VACATING AND REMANDING MINTON BARBER (CONCURS) AND TAYLOR (CONCURS) TO BE PUBLISHED 16 PAGES

* * *

KENTUCKY SUPREME COURT

2006-SC-105

DATE	EVENT	DESCRIPTION
08/30/2004	JD	JUDGMENT/ORIGINAL ACTION DATE
02/02/2006	DI	MOTION FOR DISCRETIONARY REVIEW (CIVIL) NO FILING FEE REQUIRED; COURT OF APPEALS OPINION RENDERED JANUARY 6, 2006; P DUE DATE: 03/04/2006
03/07/2006	R5	READY – DISCRETIONARY REVIEW NO RESPONSE FILED.
03/07/2006	SH	SENT OUT FOR ASSIGNMENT
03/09/2006	BCLATE	COURTS OWN MOTION: LATE LETTER RECEIVED FROM RESPONDENTS "LATE" RESPONSE TO MOTION FOR DISCRETIONARY REVIEW – RETURNED WITH LATE LETTER – DUE 3/4/06 (MAILED BY REGISTERED MAIL 3-8-06)
03/16/2006	ML	MOTION AS TO ENLARGEMENT OF TIME RESPONDENTS FILED MOTION FOR ENLARGMENT OF TIME TO FILE RESPONSE TO MOTION FOR DISCRETIONARY REVIEW. (TENDERED RESPONSE TO MOTION FOR DISCRETIONARY REVIEW) ORDER STEP #8 DUE DATE: 03/27/2006

03/28/2006	MS	SCHEDULE TO MOTION DOCKET NO RESPONSE FILED MOTION STEP #6
03/28/2006	OL	ORDER – AS TO MOT. FOR ENLARGEMENT COURT ORDER DELIVERED GRANTING RESPONDENT'S MOTION FOR ENLARGMENT OF TIME TO FILE RESPONSE TO MOTION FOR DISCRETIONARY REVIEW, TENDERED RESPONSE IS ORDERED FILED. MOTION STEP #6
07/25/2006	CKREC	** NOTICE OF RECUSAL ** THIS COURT HAVING BEEN ADVISED THAT HON. JOHN D. MINTON, JR. WAS A SITTING JUDGE IN THIS ACTION IN THE LOWER COURT, NOTICE IS HEREBY GIVEN TO ALL PARTIES THAT HE WILL NOT BE PARTICIPATING IN THIS CASE.
08/17/2006	DD	ORDER DENYING DISCRETIONARY REVIEW
08/17/2006	FL	FINALITY

NO. 03 CI 03282 **JEFFERSON CIRCUIT COURT**
DIVISION ONE (1)

GEORGE W. DAVIS and CATHERINE V. DAVIS, 1321 Garden Hill Place, Louisville, KY 40205 Individually and on behalf of others similarly situated **PLAINTIFFS**

v.

COMMONWEALTH OF KENTUCKY REVENUE CABINET and COMMONWEALTH OF KENTUCKY FINANCE AND ADMINISTRATION CABINET **DEFENDANTS**

Serve: Hon. Dana Bynum Mayton, Secretary,
Revenue Cabinet
200 Fair Oaks Lane
Suite 316
Frankfort, Kentucky 40620

Serve: Hon. Gordon Duke, Secretary, Finance and
Administration Cabinet
Room 383 Capitol Annex
Frankfort, KY 40601

Serve: Hon. A.B. Chandler III
Attorney General of Kentucky
118 State Capitol Building
700 Capitol Avenue
Frankfort Kentucky 40601

CLASS ACTION COMPLAINT FOR DECLARATORY JUDGMENT, INJUNCTION and TAX REFUNDS

Plaintiffs, George W. Davis and Catherine V. Davis, for their Complaint against the Defendants, Commonwealth of Kentucky Revenue Cabinet and Commonwealth

of Kentucky Finance and Administration Cabinet, by counsel, state as follows:

INTRODUCTION

1. Plaintiffs seek declaratory and injunctive relief and damages on behalf of themselves and all others similarly situated. Plaintiffs challenge the constitutionality of that part of the Kentucky Income Tax ("KIT"), codified at KRS 141.010, which imposes a greater KIT on interest income derived from obligations of sister states and/or their political subdivisions than on interest income derived from obligations of the Commonwealth of Kentucky and its political subdivisions. As with other tax receipts, the Revenue Cabinet deposits the income taxes collected with the Commonwealth of Kentucky State Treasurer or a depositary designated by the Treasurer pursuant to KRS 41.070.

2. The Secretary of the Finance and Administration Cabinet is the chief financial officer of the State, KRS 42.010, and said Cabinet is charged with the duty to issue its warrant to the state Treasurer for payment of authorized claims upon the State Treasury, and under KRS 141.010 as hereinafter described is a proper party through which the State maybe sued to recover wrongfully collected income tax.

JURISDICTION AND VENUE

3. This Court has subject matter jurisdiction over this action pursuant to KRS 23A.010, KRS 418.040 and KRS 452.505 because:

a. It has original jurisdiction over all justiciable causes not vested in any other court and this cause is not so otherwise vested;

b. The amount in controversy exceeds the minimum jurisdictional prerequisite of this Court;

c. Plaintiffs seek a declaration of rights concerning a justiciable controversy;

d. This action is connected with the payment of revenues into the state treasury, and

e. A prima facie violation of the Commerce Clause of the United States Constitution, Art. I, Section 8, Clause 3, is alleged, and therefore Plaintiffs had no adequate administrative remedy.

4. This Court has personal jurisdiction over the Revenue Cabinet of the Commonwealth of Kentucky (the "Revenue Cabinet"), and over the Finance and Administration Cabinet of said Commonwealth in this action because each of said Cabinets is an administrative agency of this Commonwealth subject to suit. Venue is proper in this Court pursuant to KRS 452.405 and KRS 452.505; the cause of action arose in Jefferson County and the acts of the Defendants caused and continue to cause injury to the Plaintiffs in Jefferson County.

THE PARTIES

5. George W. Davis and Catherine V. Davis are individual residents of Jefferson County, Commonwealth of Kentucky.

6. Defendant Revenue Cabinet is an administrative agency within the Commonwealth with the power to administer and enforce all tax laws of the Commonwealth.

KRS 131.030(1). Said Defendant is responsible for receiving the income tax after collection, for depositing the amounts collected with the Commonwealth of Kentucky State Treasurer and for refunding any unconstitutional taxes (KRS 134.590). Administrative agencies such as the Revenue Cabinet are not qualified or equipped to render decisions on the constitutionality of statutes and may not, therefore, settle refund claims for unconstitutional taxes made under KRS 134.590.

7. Defendant Finance and Administration Cabinet is an administrative agency of the Commonwealth within the meaning of KRS 134.590 and together with Defendant Revenue Cabinet is under a duty to refund taxes paid under a statute held unconstitutional.

THE CONTROVERSY

8. Pursuant to KRS Chapter 141 an income tax is imposed on individuals, estates, trusts, fiduciaries,[1] and corporations. *See* KRS 141.020, 141.030, and 141.040.

9. In the case of taxpayers other than corporations, the starting point for computing income subject to KIT for the tax year (generally, the calendar year) is Gross Income as defined by Internal Revenue Code ("IRC") § 61.[2] IRC

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[1] For estates and trusts, the computations of net or taxable income bases, as well as the rates of tax, are the same as those for individuals. KRS 141.030.

[2] IRC § 103 specifically provides that "gross income" within the meaning of IRC § 61 does not include interest on any "State or local bond" which is defined as "an obligation of a State or political subdivision thereof." IRC § 103(c)(1). (For purposes of § 103, the term "State" is defined to include the District of Columbia and any possession of the United States.)

§ 62 authorizes certain deductions in arriving at federal Adjusted Gross Income ("AGI"). KRS 141.020 and 141.030. Kentucky "Adjusted Gross Income" (Kentucky AGI"), in the case of taxpayers other than corporations, means gross income as defined in IRC § 61, minus the deductions allowed individuals by IRC § 62,[3] plus or minus the various additions and subtractions prescribed by KRS 141.010. The addition complained of herein is codified at KRS 141.010 (10)(c) which provides:

> "Adjusted gross income" in the case of taxpayers other than corporations means gross income as defined in subsection (9) of this section minus the deductions allowed individuals by Section 62 of the Internal Revenue Code [FN4] and as modified by KRS 141.0101 and adjusted as follows, except that deductions shall be limited to amounts allocable to income subject to taxation under the provisions of this chapter, and except that nothing in this chapter shall be construed to permit the same item to be deducted more than once:
>
> . . .
>
> (c) Include interest income derived from obligations of sister states and political subdivisions thereof[.]

KRS 141.010(10)(c),

Kentucky "net income" is the taxable income base upon which Kentucky income tax for non-corporate taxpayers is calculated. KRS 141.020 and 141 030.

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[3] KRS 141.0101 contains certain depreciation deduction modification rules that are not applicable to this case.

10. The computation of a corporation's income subject to KIT is its Gross Income as defined by IRC § 61, less the deductions allowed by Chapter 1 of the internal Revenue Code (the result being a corporation's federal taxable income), with many modifications thereto that increase or decrease federal taxable income to arrive at the amount of income subject to KIT. KRS 141.010, subds. (12)-(14). All of the modifications prescribed by the Kentucky Revised statutes are irrelevant to this case save for one. The addition complained of herein is codified at KRS 141.010(12)(c) which provides:

> (12) "Gross income," in the case of corporations, means "gross income" as defined in Section 61 of the Internal Revenue Code and as modified by KRS 141.0101 and adjusted as follows:
>
> . . .
>
> (c) Include interest income derived from obligations of sister states and political subdivisions thereof[.]

KRS 141.010(12)(c).

11. The additions required by KRS 141.010(10)(c) and (12)(c) confer upon the Commonwealth of Kentucky (and its political subdivisions) an advantage over its sister states (and their political subdivisions) by allowing Kentucky income taxpayers to exclude from KIT interest income derived from obligations of the Commonwealth of Kentucky and its political subdivisions while subjecting interest income derived from obligations of sister states and/or their political subdivisions to KIT.

12. By reason of the Commerce Clause (Article I, Section 8, Clause 3 of the United States Constitution), the

Commonwealth of Kentucky may not burden or discriminate against interstate commerce by subjecting interest on obligations of sister states and/or their political subdivisions to KIT, while exempting from income subject to KIT the interest on obligations of the Commonwealth and/or its political subdivisions. Such discrimination violates the Commerce Clause of the United States Constitution. The manner of assessment of the KIT violates the commerce Clause by providing a commercial advantage to obligations of the commonwealth of Kentucky and/or its political subdivisions at the expense of obligations issued by sister states and/or their political subdivisions. This tax scheme by its nature necessarily forecloses "tax neutral" purchase and/or sale decisions by Kentucky taxpayers. A Kentucky taxpayer (whether individual or corporate or otherwise) evaluating purchase of obligations of Kentucky (and/or its political subdivisions) and sister states (and/or their political subdivisions) can avoid or reduce KIT by buying obligations of Kentucky and/or its political subdivision, whereas such a taxpayer's income subject to KIT will be increased if the taxpayer invests or continues to hold obligations issued by sister states and/or their political subdivisions.

13. Defendants have implemented the aforementioned Kentucky Revised Statutes and have enforced, and will continue to enforce, the collection of the KIT in accordance with such statutes against the Plaintiffs and the members of the class or classes they propose to represent.

FACTS RELATING TO PLAINTIFFS' KIT TRANSACTIONS

A. Transactions Common to Multiple Plaintiffs

14. George W. Davis and Catherine V. Davis are individual residents of Jefferson County, Commonwealth of Kentucky. Plaintiffs are taxpayers who, in the course of paying their KIT, have paid KIT on interest income derived from obligations of sister states and/or their political subdivisions at various dates during the class period.

15. KRS 134.590(2) purports to require an application for refund as a condition precedent to refund of ad valorem taxes or taxes held unconstitutional, such application to be made within two (2) years from the time payment was made. The requirement is an exercise in futility because only a court may determine whether a statute or regulation is unconstitutional. An administrative agency such as the Revenue Cabinet cannot declare a statute unconstitutional.

16. Plaintiffs have filed a refund claims [sic] on behalf of themselves and all other similarly aggrieved taxpayers who paid the unconstitutional taxes at anytime during the class period.

CLASS ALLEGATIONS

17. Plaintiffs bring this action on behalf of themselves and as representatives of a class composed of all persons[4] who have paid KIT on interest income derived

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[4] The terms "person" or "persons" has the same meaning as that contained in the Internal Revenue Code of 1986. Thus the terms mean

(Continued on following page)

from obligations of sister states and/or their political subdivisions at any time during the class period, and all such persons who hereafter during all time periods for which the relief prayed for herein may be granted shall pay KIT on interest income derived from obligations of sister states and/or their political subdivisions.

18. The plaintiff Class consists of all persons (whether natural or artificial) who satisfy each of the following criteria:

a. At any time during the class period;

b. They included in their Kentucky taxable income interest income derived from obligations of sister states and/or their political subdivisions; and

c. They paid Kentucky Income Tax on interest income derived from obligations of sister states and/or their political subdivisions, or paid more Kentucky income tax, or received a lesser income tax credit, than they would have had such interest income been excluded from their Kentucky taxable income.

19. The Class period is four years, or in the alternative (if KRS 134.580 – allowing a four year claim period is held inapplicable), two years.

20. If relief is granted pursuant to KRS 134.590, Plaintiffs are entitled to refunds of the KIT paid if such tax is held to have been paid pursuant to an unconstitutional statutory scheme provided application for the

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and include an individual, a trust, estate, partnership, association, company or corporation. *See* 26 U.S.C. § 7701(a)(1).

refund is made within two (2) years after payment was made. Pursuant to KRS 134.580, however, a refund of taxes other than ad valorem and unconstitutional taxes may be made if application for the refund is made to the Revenue Cabinet within four (4) years after payment was made. This distinction violates Plaintiffs' rights of equal protection granted under the Fourteenth Amendment of the United States Constitution and under Sections 3 and 59 of the Kentucky Constitution.

21. The members of the class are so numerous that joinder of all members is impractical.

22. Plaintiffs' claims are typical of the claims of the members of the Class. All Plaintiffs were victimized by the Defendants' unconstitutional scheme to extract illegal taxes under duress.

23. There are numerous questions of law and fact which are common to the class and which predominate over any questions affecting individual members of the Class, including:

- Whether the plaintiffs are entitled to tax refunds;
- Whether the plaintiffs are entitled to interest on their tax refunds;
- Whether the additions required by KRS 141.010(10)(c) and (12)(c) violate the Commerce Clause of the United States Constitution (Article I, Section 8, Clause 3).
- Whether the 1996 amendments to KRS 134.590 that removed the "in each case" requirement allow taxpayers to maintain a class action for refunds of unconstitutional taxes without filing an application for refund "in each case."

- Whether the entire KIT, as applied to holders of obligations of obligations of sister states and/or their political subdivisions, is unconstitutional because the unconstitutional portion of the law is not severable.

- Whether the two year period under KRS 134.590 violates Plaintiffs' rights of equal protection granted under the Fourteenth Amendment of the United States Constitution and under Sections 3 and 59 of the Kentucky Constitution because KRS 134.580 allows for a longer (four years) period for refund claims.

24. Plaintiffs will fairly and adequately protect the interests of the members of the Class and have retained competent counsel experienced in class litigation. Plaintiffs are members of the class and do not have interests antagonistic to or in conflict with members of the Class. Neither Plaintiffs nor Plaintiffs' counsel have any interests which might cause them not to vigorously pursue their claims. Plaintiffs' claims are the same as those of the claims of the class, which all arise from the same operative facts and are based on the same legal theories.

25. A class action is superior to other available methods for the fair and efficient adjudication of this controversy since the membership of the Class is so numerous and so geographically widespread that joinder of all members is impracticable.

26. The prosecution of separate actions by individual members of the class would create a risk of adjudications with respect to individual members of the class which would as a practical matter be dispositive of the interest of the other members not parties to the adjudications. Defendants have acted on grounds generally applicable to

all members of the class, thereby making appropriate final injunctive and corresponding declaratory relief with respect to the class as a whole.

CLAIMS

COUNT I

Unlawful Burden on Interstate Commerce

27. Plaintiffs incorporate the above allegations in this cause of action.

28. The KIT, as applied to interest income derived from obligations of sister states and/or their political subdivisions, constitutes an unlawful burden on interstate commerce in violation of the Commerce Clause of the United States Constitution, Article I, Section 8, Clause 3, because it treats interest income derived from obligations of sister states and/or their political subdivisions less favorably than the taxation of interest income derived from obligations of the Commonwealth of Kentucky and its political subdivisions. The statutory tax scheme thus discriminates on its face against the holders of obligations of sister states and/or their political subdivisions, such as Plaintiffs, by imposing a tax and corresponding burden on such interest income that is greater than that imposed on interest income derived from obligations of the Commonwealth of Kentucky and its political subdivisions.

COUNT II

Uniformity and Equal Protection

29. Plaintiffs incorporate the above allegations in this cause of action.

30. Section 171 of the Kentucky Constitution requires taxes to "be uniform upon all property of the same class subject to taxation . . . " Section 3 of the Kentucky Constitution and the Fourteenth Amendment to the United States Constitution grant equal protection of the laws to all persons. The KIT, as applied to the transactions complained of herein, violates these requirements because it does not tax in-state interest and out-of-state interest, otherwise similar in economic substance, at the same rate. Instead, it taxes the out-of- state interest at a higher rate than in-state interest.

COUNT III

The Entire KIT is Unconstitutional

31. Plaintiffs incorporate the above allegations in this cause of action.

32. If, as a practical matter, the admitted unconstitutional portion of the law is not severable, then the entire KIT is unconstitutional.

COUNT IV

Refunds

33. Plaintiffs incorporate the above allegations in this cause of action.

34. The Plaintiffs and members of the class or classes they represent have been, are, and shall be (as the case maybe) required to pay, without predeprivation remedies, KIT on out-of-state interest, upon pain of suffering criminal fines and penalties for non-payment of said tax, KRS 141.990.

35. From 1993 (perhaps earlier) to 1996, KRS 134.590 (or its predecessor) required that a [sic] application for refund be made "in each case" thereby effectively precluding class actions for tax refunds under KRS 134.590 (or its predecessor). The "in each ease" requirement was removed from KRS 134.590 in 1996 effective for taxable years beginning after December 31, 1995. (Effective for "taxable years beginning after December 31, 1995." Compiler's Notes, Section 11 of Acts 1996, ch. 344.) KRS 134.590 applies to the refund of taxes held unconstitutional. No protest is required. When a statute is held unconstitutional, however, the agency "shall refund the money" paid under color of the unconstitutional statute, with no provision for limiting said repayment to the "part thereof . . . wrongfully collected." Class members who paid the illegal taxes at any time during the class period are entitled to the greater of (a) a refund of all KIT paid if the KIT statute is held unconstitutional or (b) if the KIT statute is held severable, the part thereof of the KIT wrongfully collected.

36. If the Defendants cannot provide Plaintiffs the relief sought under KRS KRS [sic] 134.590, if that statute is held to allow recovery only for the illegal tax increment, then all KIT paid by taxpayers at any time during the class period must be disgorged.

37. As a result of the many thousands of unlawfully taxed transactions, Plaintiffs and each class member are entitled to tax refunds as set forth herein.

WHEREFORE, Plaintiffs demand judgment against Defendants:

A. Certifying this action as a class action and designating plaintiffs as class representatives and plaintiffs' counsel as class counsel;

B. Declaring that the additions required by KRS 141.010(10)(c) and (12)(c) violate the United States Constitution and the Constitution of the Commonwealth of Kentucky and are therefore null and void insofar as they relate to the transactions of the Plaintiffs and the class or classes as described herein;

C. Restraining and permanently enjoining and prohibiting Defendants from collecting or attempting to collect the KIT on interest income derived from obligations of sister states and/or their political subdivisions;

D. Declaring that Plaintiffs and the members of the class they represent are entitled to refunds of any KIT they have paid as a result of being obligated under color of law to pay KIT on interest income derived from obligations of sister states and/or their political subdivisions; and,

E. Any and all other relief to which they may be entitled.

Dated: Louisville, Kentucky

April 11, 2003

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COMMONWEALTH OF KENTUCKY
JEFFERSON CIRCUIT COURT
DIVISION 3
CIVIL ACTION NO. 03-CI-03282

GEORGE W. DAVIS AND
CATHERINE V. DAVIS **PLAINTIFFS**

VS. **ANSWER**
(Filed May 5, 2003)

REVENUE CABINET,
COMMONWEALTH OF
KENTUCKY, et al **DEFENDANTS**

* * *

First Defense

1. As to ¶ 1 of the Complaint, the Defendants admit that this paragraph characterizes the general nature of the claims that appear to be asserted, and the relief that appears to be demanded by the Plaintiffs, in the Complaint. The Defendants admit the last sentence of this paragraph. The Defendants deny that the Plaintiffs are entitled to the relief requested or referred to in this paragraph and in this Complaint generally and they deny that the Plaintiffs' claim(s) is (are) valid or well-founded.

2. As to ¶ 2 of the Complaint, the Defendants admit that KRS 42.012, but not KRS [illegible] as the Plaintiffs allege, states that "[t]he secretary of the Finance and Administration Cabinet shall be the chief financial officer of the state." The Defendants deny that the Secretary of the Finance and Administration Cabinet is a proper party through which the State may be sued to recover wrongfully collected income tax. The Defendants would deny, based upon sovereign immunity, Ky. Const. §§ 230 and

231, and relevant statutory provisions and case law, that any Kentucky income taxes previously paid by the Plaintiffs or by any one else may be recovered through an action such as that brought by this Complaint. The Defendants would admit that the Finance and Administration Cabinet is charged with the duty to issue a warrant to the State Treasurer for payment of authorized claims upon the State Treasury.

3. As to ¶ 3 of the Complaint, the Defendants would admit that there is case law to support the proposition that this Court would have subject matter jurisdiction over this action to the extent it attacks the constitutionality of the statutory provisions in question on their face. *See e.g., Commonwealth v. DLX, Inc.*, Ky., 42 S.W.3d 624 (2001). Subject matter jurisdiction is a defect or defense that cannot be waived, however, and whether a decision such as *DLX* would apply in the legal context to which this action relates must necessarily depend upon further review of existing and future case law. Accordingly, the Defendants are without Knowledge or information sufficient to form a belief as to the truth of the Plaintiffs' assertion of subject matter jurisdiction on this basis. The Defendants would admit that under KRS 23A.010 this Court is "a court of general jurisdiction [that] has original jurisdiction of all justiciable causes not exclusively vested in some other court." The Defendants are without knowledge or information sufficient to form a belief as to the truth of the Plaintiffs' assertion that jurisdiction of the subject matter of this action is not vested elsewhere – e.g., the procedure set forth in 103 KAR 1:010; KRS 131.110; 131.340; 131.370. The Defendants deny the implication of the allegation in this paragraph that "[t]he amount in controversy exceeds the minimum jurisdictional *amount*

prerequisite of this court" – namely, that this action properly seeks damages against the Defendants. This action, to the extent it seeks damages or tax refunds, cannot be brought against the Defendants because there has been no consent or waiver of sovereign immunity by the General Assembly to or for this kind of action against the Commonwealth. *See also* Ky. Const. §§ 230, 231. The Defendants would admit that the Plaintiffs seek a declaration of rights in the Complaint but are without knowledge or information sufficient to form a belief as to the truth of the Plaintiffs' assertion that they seek a declaration of rights concerning a justiciable controversy. The Defendants deny that this Court would have subject matter jurisdiction over this action under KRS 452.505 because it is connected with the payment of revenues into the state treasury. For the reasons previously stated, if this Court has subject matter jurisdiction, it would be limited to declaratory and injunctive relief with respect to the facial validity of the statutory provisions challenged in the Complaint. The Defendants deny that "[a] prima facie violation of the Commerce Clause of the United States Constitution, Art. I, Section 8, Clause 3, is alleged, and therefore Plaintiffs have no adequate administrative remedy."

4. As to ¶ 4 of the Complaint, the Defendants admit that this Court has *personal* jurisdiction over them because of the Plaintiffs' compliance with CR 4.04(6) and not because they are administrative agencies of this Commonwealth subject to suit. Whether the Defendants are truly subject to suit and to this action in particular will depend upon the applicability of a variety of principles or provisions of law. The Defendants are without knowledge

or information sufficient to form a belief as to the truth of the allegations in the last sentence of this paragraph.

5. The Defendants are without knowledge or information sufficient to form a belief as to the truth of ¶ 5 of the Complaint.

6. The Defendants would admit that the Revenue Cabinet administers and enforces most, but not all, of the tax laws of the Commonwealth, including the income tax. *See, e.g.,* KRS 131.030(1); *see also Bob Hook Chevrolet Isuzu, Inc. v. Transportation Cabinet,* Ky., 983 S.W.2d 488 (1998). The Defendants admit the second sentence of ¶ 6 of the Complaint. The Defendants deny the last sentence of ¶ 6 of the Complaint. *See, e.g.,* KRS 131.020(2); 131.030(3); *Reeves v. Gerard,* Ky., 255 S.W.2d 21 (1953).

7. The Defendants deny ¶¶ 7, 11 and 12 of the Complaint.

8. The Defendants admit ¶¶ 8, 9 and 10 of the Complaint with the qualification that the income tax statutes speak for themselves and would prevail over the Plaintiffs' characterization or description of them in these paragraphs. Furthermore, there may be other provisions of law or other facets of the statutory provisions referred to in these paragraphs that may be or become relevant to this case as it progresses and the admissions made in this paragraph of this Answer should not be construed as ruling out the Defendants' utilization of those other provisions of law at a later date where appropriate. As to ¶ 9 of the Complaint, the Defendants would deny that KRS 141.020 and 141.030 are the appropriate citations to support the second sentence of this paragraph. Instead, it would appear that KRS 141.010(10) and (11) would be the more appropriate citations.

9. As to ¶ 13 of the Complaint, the Defendants admit that they are applying and will apply the Kentucky income tax statutes as written to all persons covered by or subject to the terms of those statutes. They deny that the Plaintiffs may represent any class or members of any class.

10. The Defendants are without knowledge or information sufficient to form a belief as to the truth of ¶ 14 of the Complaint.

11. The Defendants deny ¶ 15 of the Complaint. The Defendants would further note that 134.590 does not merely "purport" to require an application or claim for refund within two years of payment of the taxes whose refund is sought as a condition precedent to a refund of unconstitutional taxes but does in fact require such an application for refund as a condition precedent to a refund of unconstitutional taxes, both by virtue of its plain language and controlling judicial precedent.

12. As to ¶ 16 of the Complaint, the Defendants are without knowledge or information sufficient to form a belief as to the truth of the allegation that the Plaintiffs have filed refund claims. The Defendants have not been able to locate any such refund claims as of yet. The Defendants deny that any such refund claims could be properly or lawfully filed by the Plaintiffs on behalf of anyone else. The Defendants further deny that the Plaintiffs or anyone else have paid any Kentucky income tax that is unconstitutional. The Defendants also deny the validity, propriety, or legality of the "class period" concept utilized by the Plaintiffs in this paragraph.

13. As to ¶¶ 17-26, the Defendants deny that this action may properly or lawfully be maintained as a class action and assert that class certification is neither

necessary or appropriate in this case. The Defendants admit that ¶¶ 17 and 18 accurately characterizes and describes what the Plaintiffs are attempting to do by these paragraphs and the class they seek to represent; however, the Defendants deny that the class certification or class action determination sought by the Plaintiffs is lawful, proper, or warranted and they deny the validity, propriety, or legality of the "class period" concept utilized in these paragraphs. As to ¶ 19 of the Complaint, the Defendants deny the implication made therein that the four year time limitation prescribed by KRS 134.580 would govern refunds based upon the constitutional claims asserted by the Plaintiffs in the Complaint and would further assert that KRS 134.590 sets forth the time limitation that would apply in the event the Plaintiffs' claims were determined to be meritorious. The Defendants deny the last sentence of ¶ 20 of the Complaint. As to ¶ 20 of the Complaint, the Defendants would admit that the first two sentences generally or roughly describe the operation of KRS 134.580 and 134.590, except that they would deny any assertion or suggestion that any amount refunded under either of these statutes, and especially KRS 134.590, would be the entire amount of tax paid by a taxpayer for the tax year in question. Furthermore, the language of KRS 134.580 and 134.590 and any relevant judicial precedent construing them would control any question as to these statutues' meaning and effect. The Defendants are without knowledge or information sufficient to form a belief as to the truth of ¶ 21, the first sentence of ¶ 22, and ¶¶ 23-26. The Defendants deny the second sentence of ¶ 22.

14. As to ¶¶ 27, 29, 31 and 33 of the Complaint, the Defendants hereby incorporate their responses to the allegations these paragraphs incorporate.

15. The Defendants deny ¶¶ 28, 30, and 32 of the Complaint.

16. As to ¶ 34 of the Complaint, the Defendants admit that there are criminal penalties that relate to the income tax, but they would deny the implication of this paragraph that mere nonpayment of the tax triggers these criminal penalties. The Defendants deny that the Plaintiffs properly represent a class. They are without knowledge or information sufficient to form a belief as to the truth of the allegation that the Plaintiffs. are paying income tax "on out-of-state interest." As for the Plaintiffs' assertion in this paragraph that this payment was made "without predeprivation remedies," the Defendants would acknowledge that *Revenue Cabinet v. Gossum,* Ky., 889 S.W.2d 329 (1994) may tend to indicate that this is indeed the case. However, this is in the final analysis a question of law and there may be subsequent or other legal developments that may call for a different conclusion or that may provide support for a good faith argument for reversal or modification of *Gossum.* Accordingly, the Defendants are without knowledge or information sufficient to form a belief as to the truth of this "without predeprivation remedies" allegation.

17. As to ¶ 35 of the Complaint, the Defendants deny that class actions for tax refunds are permitted under KRS 134.590 in either its present form or its previous versions and deny the correctness of the Plaintiffs' Interpretation of the effect of the 1996 amendment to KRS 134.590. The Defendants admit that KRS 134.590 applies to the refund

of taxes held unconstitutional in accordance with its terms and as construed by the Kentucky courts. The Defendants deny that "[n]o protest is required." While no protest is required at the time of payment of the taxes, as in the case of KRS 138.500, a protest is required if the Cabinet denies a refund claim. *See* 103 KAR 1:010 § 2. The Defendants deny the last two sentences of ¶ 35 of the Complaint.

18. The Defendants deny ¶¶ 36 and 37 of the Complaint. They further assert that tax refunds may not be obtained from the Commonwealth by or through an action such as this. Such an action is an unauthorized suit against the Commonwealth and barred by sovereign immunity and Ky. Const. §§ 230 and 231.

19. The Defendants deny that the Plaintiffs are entitled to any of the relief requested in the Plaintiffs' demand for judgment.

20. Any allegation in the Complaint not specifically admitted above is hereby denied.

Second Defense

The Complaint fails to state a claim upon which relief can be granted.

Third Defense

The Plaintiffs lack standing.

Fourth Defense

This Court lacks jurisdiction over the subject matter.

Fifth Defense

This action is an unauthorized suit against the Commonwealth barred by sovereign immunity and Ky. Const. §§ 230 and 231.

Sixth Defense

Any ruling that the statutory provisions assailed by the Plaintiffs as unconstitutional are indeed unconstitutional should be made prospectively based upon the principles recognized in such cases as *Chevron Oil Co. v. Huson,* 404 U.S. 97 (1971) and *Yount v. Calvert,* Ky. App., 826 S.W.2d 833 (1991).

Eighth Defense

The Plaintiffs have failed to exhaust their administrative remedies. Exclusive original jurisdiction of tax controversies is vested in the Kentucky Board of Tax Appeals.

Therefore, based upon the foregoing, the Defendants request the following:

1. Dismissal of the Complaint with prejudice or a judgment in the Defendants' favor on the claims asserted in the Complaint that denies the Plaintiffs any relief or recovery against or from the Defendants.
2. An award to the Defendants of their costs and other expenses;
3. Denial of the Plaintiffs' request that this action be maintained as a class action;

4. Any and all other relief to which the Defendants may appear entitled.

Respectfully submitted

/s/ Doug Dowell
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CERTIFICATE OF SERVICE

I hereby certify that a true copy of the foregoing Answer was served upon M. Scott Barrett and Dennis T. Trainor, Barrett & Associates, 30 North LaSalle Street, Suite 3900, Chicago, Illinois 60602; Donn H. Wray, Stewart & Irwin, 251 East Ohio, Suite 1100, Indianapolis, Indiana 46204-2118; Hart L. Robinovitch, Zimmerman Reed P.L.L.P., 14646 N. Kierland Blvd., Suite 145, Scottsdale, Arizona 85254 and Irvin D. Foley, David W. Gray, and Anthony D. Raluy, Foley, Bryant & Holloway, Kentucky Home Life Building, 239 South Fifth Street, Suite 1700, Louisville, Kentucky 40202 by first-class mail on this the 5th day of May, 2003.

/s/ Doug Dowell
Douglas M. Dowell
Revenue Cabinet